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INFO RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION PRIORITY
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RUEHFK/AMCONSUL FUKUOKA PRIORITY 3501
RUEHNH/AMCONSUL NAHA PRIORITY 5843
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RUCPDO/USDOC WASHDC PRIORITY
RHMFISS/USFJ PRIORITY
RUEHGV/USMISSION GENEVA PRIORITY 3500
RUEHBS/USEU BRUSSELS PRIORITY
RHEHAAA/WHITE HOUSE WASHDC PRIORITY
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C O N F I D E N T I A L SECTION 01 OF 03 TOKYO 000850

SIPDIS

TREASURY IA FOR DOHNER, WINSHIP, FOSTER;
STATE EEB/IFD AND EAP/J;
DEPT PASS USTR FOR CUTLER, BEEMAN;
NSC FOR DANNY RUSSELL AND JIM LOI

E.O. 12958: DECL: 04/13/2019
TAGS: [ECON](#) [EFIN](#) [PGOV](#) [JA](#)
SUBJECT: CABINET APPROVES SUBSTANTIAL NEW FISCAL STIMULUS

REF: REF: A) TOKYO 764

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Classified By: CDA James Zumwalt for reasons 1.4 (b) and (d).

11. (C) Summary: Prime Minister Aso announced April 10 a new \$568 billion headline figure Japanese government fiscal stimulus package entitled "Countermeasures Against Economic Crisis". The package will be implemented in the form of a fiscal year 2009 supplemental budget submitted to the Diet in late April, and appears more substantial than its three predecessors, both in actual cost (\$154 billion) and in impact on GDP (2%). The package's stated objective is to put the economy back on a sustainable growth path by fiscal year 12010. Aso described the plan as justified by Japan's sharp economic downturn and explicitly called it Japan's response to the G20 Leaders' call for "concerted fiscal expansion." Embassy contacts note that Aso's success in gaining passage of the supplementary budget could influence his decision to dissolve the Lower House for a snap election. End Summary.

Three Key Metrics

12. (C) There are three key metrics of the package's size: the headline figure -- the least meaningful measure -- is JPY56.8 trillion (\$568 billion, or 11% of GDP). The second metric, the cost in terms of new actual government expenditure is JPY15.4 trillion (\$154 billion, or 3% of GDP), the largest ever for a supplemental budget. The third metric, the "real water" anticipated impact on final demand appears, by FINATT estimate, to be around 1.9% of GDP over 2009 and 2010. (Note: The largest supplemental budget until now had been the JPY7.6 trillion fiscal year 1999 second supplemental under then Prime Minister Obuchi. End Note.)

13. (C) The Cabinet Office itself projects that the package will add 2% of GDP in fiscal year 2009 and that "the effects will continue through fiscal year 2010," helping to avoid the risk of a "negative spiral", and create 400,000-500,000 jobs over the next year. Japan's output gap was 4.1% of potential GDP in Q4 2008, according to the Cabinet Office, but the IMF, OECD, and other analysts forecast it will rise

to around 10% of GDP in 2009 in the absence of further fiscal stimulus.

Composition

¶4. (C) The stimulus' overall headline figure comprises 16.4 trillion yen in fiscal spending measures and JPY41.8 trillion in financial measures. The major fiscal measures are infrastructure spending (JPY 3.8 trillion), health measures (JPY 2.8 trillion), and employment measures (JPY 2.5 trillion). Financial measures center on support for corporate financing through larger government loans and loan guarantee programs. In response to the current "exceptional" stock market conditions, the package calls for consideration of outright stock purchases by an unspecified government entity.

¶5. (C) The package divides its stimulus measures into four sections: 1) "emergency" measures to prevent a free-fall of the economy, such as employment measures, financial measures, and the front loading of public works; 2) steps to increase future potential growth, including a "Low Carbon Revolution", health promotion initiatives, IT and infrastructure development; 3) measures to give the public a sense of "security and vitality", including regional revitalization, consumer safety, and social security measures; and 4) taxation, featuring a temporary reduction in the gift tax, reduced taxes for SMEs, and an extension of tax incentives for R&D.

Summary Table of "Countermeasures Against Economic Crisis"

	New Spending And Financial	New Final Demand
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	Measures (Headline Figure) (Trillion Yen)	Estimate (Real Water)
¶A. Fiscal Spending Measures	16.4	9.7
1) Infrastructure Spending	3.8	3.2
2) Health Promotion Measures	2.8	1.4
3) Strengthening Employment	2.5	1.3
4) Grants to Local Governments	2.4	1.2
5) Alleviating Peoples, Concerns	2.2	1.1
6) Environmental Measures	2.2	1.1
7) Regional Economic Renewal	0.4	0.3
8) Tax Cuts	0.1	0.05
¶B. Financial Measures	41.8	0
1) JFC, DBJ, Shoko Chukin Loans	13.4	0
2) Loan Guarantees Increases	10	0
3) Other Measures	18.4	0
¶C. Total	56.8	9.7
(Percent of GDP)	11.1	1.9

(Note: The overall headline figure does not sum due to JPY1.4 trillion in overlapping measures. Infrastructure spending is estimated to include roughly 15% of land acquisition costs, which do not contribute to increased spending on a national accounts basis. Roughly 50% of both subsidies and grants to local governments are assumed to add to new final demand. For a gift tax cut, the marginal propensity to consume is assumed to be about 0.52, based on the average rate between 1981 and 2007; increased loans and loan guarantees are assumed to not add to final new demand. End Note)

Financing

¶6. (C) The GOJ will primarily use issuance of new government bonds (JGB) to finance the new supplemental. However, emergency reserves set aside in the regular budget for FY09 (which contained an unprecedented 1 trillion yen in special reserves for unexpected economic events that require an

immediate government response) and reserves held by the Fiscal Loan Fund Special Account will also help fund the package. (Note: that the rise in the benchmark 10-year JGB yield to a five-month high of 1.48% April 9 has been partly attributed to increased concern over the government's fiscal conditions. End Note.)

Next Steps

17. (C) The Ministry of Finance will now take the Cabinet approved policy package and compile a FY09 supplemental budget for submission to the Diet by the end of April, which will likely be the fastest supplemental budget in Japan's history. The opposition Democratic Party of Japan (DPJ), which through its control of the Upper House of the Diet could substantially delay adoption of the FY09 supplemental, has not officially reacted. The DPJ favors higher spending, but will have to choose between two political risks: lending support to a ruling party initiative or appearing to be blocking stimulus. Either way, an end of April submission to the Diet likely will require Prime Minister Aso to extend the current ordinary session to ensure the stimulus measure is passed.

18. (C) Comment: Prime Minister Taro Aso is clearly trying to get ahead of events and to demonstrate to the international community that Japan is a leader in the global response to the economic crisis. But in addition to taking steps to reverse the slide in Japan's economy -- some experts predict the country's GDP could fall more than 6% in 2009-- Aso is also playing a domestic political game. Through the new stimulus proposal, Aso appears to be positioning himself in case he decides to use Diet deliberations over the supplemental budget as a pretext for calling a snap general election in May. Senior Diet contacts tell the Embassy they

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do not expect an election to be called before August at this point, but acknowledge that the timing could be linked to the supplementary budget. Post will analyze the specific components of the Aso Cabinet's stimulus measures and report Septel.
ZUMWALT